
PERSPECTIVES

TOYING WITH FRAUD AND
PLAYING WITH CONSEQUENCES



Our perspectives feature the viewpoints of our subject matter experts on current topics and emerging trends.

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In July 2023, one of the year's most anticipated movies, the Barbie movie, premiered in theaters, achieving more than USD1 billion in global ticket sales¹. One potentially overlooked detail in the movie was the character Ruth, who appeared to live on the 17th floor of Mattel's headquarters, and who mentioned getting into trouble with the Internal Revenue Service. The character Ruth was, in fact, paying homage to Barbie's creator, Ruth Handler. Mrs. Handler was one of the co-founders of Mattel and created the Barbie doll in 1959, which was inspired by her daughter, Barbara.² Given the adoration Barbie has garnered over the years since her creation, you might ask yourself, how could she possibly be involved in a fraud case? While the Barbie movie correctly depicted Ruth facing trouble, it inaccurately identified the agency involved; it was the Securities and Exchange Commission, not the IRS. Mrs. Handler, among others, were charged with conspiracy and making false financial statements by overstating revenues and income between 1971 and 1973, which Mattel ultimately admitted to in 1974.³ The reason for Mattel's fraudulent actions was to influence the market price of their stock. Mrs. Handler was sentenced to 500 hours of community service per year and five years of probation.⁴

Unfortunately, the Handler case is not the sole instance of a toy company being accused of fraudulent activities. Over the years, the toy industry has seen several notable fraud cases, including those involving prominent toy companies, such as Toys "R" Us, Funko, Inc., Hasbro, Inc., LeapFrog Enterprises, Inc., and Tyco International. While it is not feasible

to discuss all of them, we have selected two particularly interesting cases to highlight.

In the Toys "R" Us fraud case, which was filed in 2020, executives were accused of making false representations to secure loans during bankruptcy, which they filed for in 2017. These false statements included misrepresenting the company's sales projections and its viability as a going concern, leading to significant financial losses. The former executives and board members were accused of giving preference to their own financial interests over those of the creditors during the company's bankruptcy. Allegations included making false representations to secure loans for a costly restructuring, while knowing they couldn't meet the terms, and timing bonuses to circumvent bankruptcy rules.⁵ This case was ultimately resolved in 2022, though the terms of the settlement remain confidential.⁶

The LeapFrog fraud case centered around allegations that the company misrepresented its financial health, which misled investors and stakeholders. It was alleged that they inflated their sales projections for the fiscal year of 2003 by either failing to disclose or misrepresenting several key issues that could impact their projected earnings. In October 2003, LeapFrog announced that they had failed to meet their sales projections, resulting in a significant 25% decline in their stock. A class-action lawsuit was filed in April 2005, citing violations of the Securities Exchange Act of 1934, resulting from false and misleading statements and omissions. This case was ultimately resolved in 2008, with LeapFrog agreeing to a settlement of USD2.3 million.⁷

These incidents draw attention to the importance of strong corporate governance,

¹ <https://www.today.com/video/-barbie-hits-1-billion-at-box-office-breaking-record-190197829599>

² <https://corporate.mattel.com/history>

³ <https://www.businessinsider.com/barbie-inventor-ruth-handler-mattel-irs-sec-false-financial-statements-2023-7>

⁴ <https://www.museumofplay.org/app/uploads/2022/01/2-3-book-review-5.pdf>

⁵ <https://www.forbes.com/sites/joanverdon/2022/01/20/former-toys-r-us-execs-board-accused-of-fraud-in-bankruptcy-decisions/>

⁶ <https://www.retaildive.com/news/toys-r-us-creditors-reach-resolution-former-execs-lawsuit-bankruptcy/634240/>

⁷ <https://securities.stanford.edu/filings-case.html?id=102926>

ethical practices, and rigorous regulatory compliance in maintaining the integrity and trustworthiness of not only the toy industry but for all companies. Due to fraudulent activity, companies can experience significant consequences, including reputational damage, financial losses, and regulatory scrutiny.

However, the repercussions of fraud can extend beyond the company responsible, including:

- » Investors and stakeholders can incur significant financial losses due to poor investment decisions based on falsified or misrepresented information. They could also suffer financial losses due to a decline in the company's stock value and suspension of dividends if the company ends up in financial distress. If investors or stakeholders are companies, this can cause their own financial statements to be impacted as well.
- » Employees could lose their jobs if the company collapses. Investments in company stock or retirement plans can also result in personal financial losses to the affected employees.
- » Toy manufacturers may also be adversely affected by fraudulent activities of companies selling their products. They could extend credit or invest their own resources based on false information from these companies. This could lead to financial losses to the manufacturer, including nonpayment for delivered products and legal costs, among other expenses.
- » Public trust can be impacted due to the widespread media coverage of companies charged with fraud. Public sentiment can turn on a company, which could lead to further economic losses by the public boycotting the company.

The takeaway from these types of fraud cases is the extensive and detrimental impact they have not only on the companies committing the fraud but also on the broader environment. Fraud perpetrated by companies distorts

market perceptions, causing inefficient capital allocation, which can have a ripple effect on the overall economy.

While public companies (and others) may require annual financial statement audits, which have an affirmative duty to address the risk of fraud, only 3% of all occupational frauds are discovered from financial statement audits, internal audits discover 14% of frauds and tips comprise 43% of all occupational frauds.⁸ For CPAs, the implications are significant, with increased scrutiny and potential legal liability. As CPAs, our responsibility is to ensure the accuracy and reliability of financial reporting to protect the interests of the public and the integrity of the financial markets. A few key practices CPAs can implement to contribute to this include adhering to professional standards and ethical guidelines, as provided in the AICPA's Code of Professional Conduct; establishing strong internal controls; segregation of duties; maintaining effective communication; and keeping their education up to date, which is ever-changing and becoming more challenging with new technologies.

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⁸ [2024-report-to-the-nations.pdf](#)

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